costs would exceed the benefits.[46] The simple certification procedure adopted by Congress allows franchising authorities to respond in a timely manner should the need arise in the future.[47] Thus, the Commission satisfies its obligation to ensure reasonable rates in communities that choose not to regulate by offering an expedient certification process and an administratively simple basic rate formula. Congress has not clearly preempted a state's authority over its subdivisions[48] and the FCC has no authority to disturb a state's sovereign powers.

Similarly, contractual franchise agreements where the franchising authority has agreed not to regulate rates remain in full force under the 1992 Cable Act. Austin, TX argues that these agreements are preempted by the 1992 Cable Act.[49] However, the statute does not expressly preempt franchise agreements or other valid contracts. Further, as tentatively concluded in paragraph 14 of the Notice, and explained above, if franchising authorities choose not to certify, there is no rate regulation.

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[46]Cable operators would also face lower costs without local regulation. Yet, the threat of regulation under a simple certification process should force the operator to keep its prices low in order to avoid future regulation. Thus, the threat of regulation operates in an analogous fashion to the threat of competition, as under the contestability principle. See Fleischman and Walsh Comments at 28-29.

[47]The concern that some communities may not have adequate resources to regulate rates, as expressed in the NATOA Comments at 21, can be resolved by using a simple benchmark approach, as advocated by the Commenters, in which the city need only compare the operator's rates with the benchmark established by the FCC.

[48]For a discussion of this preemption issue, see Fleischman and Walsh Comments at 34-36.

[49]Austin, TX Comments at 35.

Therefore, an agreement not to regulate is consistent with the 1992 Cable Act and is not preempted.[50]

Some parties claim that unless FCC jurisdiction is broadened to include communities that cannot qualify for certification, these communities will engage in sham certification filings in order to establish FCC jurisdiction.[51] However, FCC jurisdiction is not proper in those cases. First, if the community does not qualify, for example, because it lacks the personnel or other resources necessary for rate administration,[52] the FCC cannot qualify in its place.[53] Second, the FCC is not intended to act as a permanent regulatory body engaged in the details of rate

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[50]There is no explicit language in the 1992 Cable Act which preempts franchise agreements to not regulate rates. Therefore, federal preemption occurs when Congress intends exclusive federal regulatory control of basic cable rates or when the state law is inconsistent with federal law. Cable Television Association of New York v. Finneran, 954 F.2d 91, 95 (2d Cir. 1992). Because local authorities can choose not to regulate, federal law does not preempt state contract law under either preemption test.

[51]Coalition of Municipal and Other Local Governmental Franchising Authorities Comments at 7, 11-12 (lack of economic resources may prevent communities from qualifying); MFA Comments at 5-6.

[52]47 U.S.C. § 543(a)(3).

[53]47 U.S.C. § 543(a)(6) limits FCC jurisdiction; "the Commission shall exercise the franchising authority's regulatory jurisdiction." As a "solution" to the problem of sham certifications, some parties recommend that unqualified franchising authorities notify the FCC so that the Commission will assert jurisdiction over local basic rates. MFA Comments at 12; Coalition of Municipal and Other Local Governmental Franchising Authorities Comments at 12. However, the jurisdictional limits on the FCC do not permit it to assume such a role; it is also patently unfair for these communities to foist the costs of regulation on the federal government.

regulation for communities across the nation.[54] Moreover, if the FCC adopts a simple benchmark approach, as recommended by the Commenters, the costs of regulation should be minimal.

The Commenters agree with the FCC's proposal in paragraph 17 of the Notice that the franchising authority must show evidence of lack of effective competition as part of the certification procedure. Some parties argue that the franchising authority should not be required to show a lack of effective competition.[55] However, regulation is permitted only when a lack of effective competition is shown. The statute requires that the FCC find that the cable system is not subject to effective competition.[56] The franchising authority has the duty to certify that it has legal authority to regulate; such legal authority does not exist unless the FCC finds a lack of effective competition.[57] Therefore, the obligation to show a lack of effective competition rests with the franchising authority.[58] However, as explained in

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[54]The Commission is meant to exercise only interim regulatory jurisdiction until the franchising authority qualifies to file a new certification. Coalition of Municipal and Other Local Governmental Franchising Authorities Comments at 12. If the franchising authority has no intention of qualifying, this is an abuse of the certification process and interim FCC jurisdiction is not meant to apply.

[55]Austin, TX Comments at 31-32; NATOA Comments at 24-25; MFA Comments at 13-14.

[56]47 U.S.C. §543(a)(2).

[57]Id. at §§ 543(a)(2), (3).

[58]Even some comments on behalf of regulatory interests agreed that the franchising authority should bear the burden of demonstrating a lack of effective competition. See Schaumburg, IL Comments at 4; State of New Jersey Board of Regulatory Commissioners Comments at 24-25.

the Commenters' section on the effective competition tests, the FCC should require other multichannel video programming distributors to report annually to the Commission on their subscriber base and service areas so that both the franchising authority and the FCC have accurate sources of information.

Lastly, the Commenters ask that the FCC accord cable operators the due process rights during certification, revocation, and local regulation procedures. The cable operator should be given the right to directly inform the Commission of effective competition during the certification procedures. Because the 1992 Cable Act establishes a preference for competition,[59] cable operators should be permitted to show the presence of effective competition to the FCC before it is burdened with inappropriate rate regulation. NATOA suggests that revocation or any other remedy should not result when the franchising authority departs from its regulatory plan in its certification, as long as regulations do not substantially impair the implementation of FCC regulations.[60] However, the cable operator needs to make business decisions on the basis of the franchise authority's stated regulatory approach in the certification.[61] Thus, the FCC must, in fairness, revoke or at

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[59]47 U.S.C. § 543(a)(2). A cable operator's challenge could be limited to a submission of a written statement, which would avoid the delays of "a full pleading cycle," a concern of the FCC at paragraph 23 of the Notice.

[60]NATOA Comments at 35-36.

[61]The FCC proposes in paragraph 23 of the Notice to require that the certification be served on the cable operator. Thus, the operator should be entitled to rely on the statements in an approved certification.

least suspend the franchise authority's power to regulate when it deviates from the regulatory statements in the certification and this deviation substantially impacts on the cable operator. The cable operator should be permitted to bring a revocation proceeding to show such a negative impact. In addition, when a certified franchising authority fails to regulate for a substantial period of time and then, without notice reimposes regulation, the cable operators' justified business expectations are materially affected. Such sporadic regulation does not ensure reasonable rates in the long term and should be grounds for revocation.

C. Basic Rate Formula.

1. Benchmarks Were Widely Preferred Over Rate Of Return Regulation.

As the Commenters have explained in detail, and as many other parties agreed, the Commission and other state and federal agencies have correctly rejected rate of return (cost-based or cost of service) regulation because of its many flaws.[62] While some parties nevertheless argued that cost-based regulation is the preferred alternative,[63] this type of regulation has been roundly criticized for discouraging risk taking and innovation, encouraging rate base padding, increasing incentives to cross-subsidize, and, if adopted, resulting in an administrative

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[62]See Fleischman and Walsh Comments at 46-49.

[63]See, e.g., CFA Comments at 79; League of California Cities Comments at 15; City of Rocky Mount, NC Comments at 2; Austin, TX Comments at 11 (proposes cost of service regulation after temporary benchmark period during which cost information can be gathered); Coalition of Municipal and Other Local Governmental Franchising Authorities Comments at 29.

nightmare for the Commission.[64] MCATC's comments described its failed experience with cost of service rate regulation, and it now endorses a benchmark approach.[65] Indeed, the Commission's proposed benchmark approach was widely embraced by numerous municipal franchising authorities, cable operators, and other groups.[66]

Some parties argue that municipalities should be able to elect between benchmarks and cost of service regulation.[67] The flaws of cost-of-service regulation are just as evident where it is an option rather than the only regulatory alternative. Moreover, the fact that Congress has directed the Commission to establish formulas and standards for basic rate regulation[68] and has provided for cable operators to appeal to the Commission to revoke local jurisdiction when such formulas and standards are not being followed[69] indicates that Congress has mandated a

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[64]See, e.g., Fleischman and Walsh Comments at 46-50; Time Warner Comments at 14-20; Continental Cablevision ("Continental") Comments at 26; Cablevision Industries Corporation Comments at 12-14; Cox Cable Communications ("Cox") Comments at 8-11.

[65]MCATC Comments at 7.

[66]See, e.g., City of Tallahassee, FL Comments at 2; League of Kansas Municipalities Comments at 1; City of Mesa, AZ Comments at 4; City of Marshfield, WI Comments at 2; Cities of Inverness, FL et al. Comments at 1-2; Leesburg, FL Comments at 1; City of Thousand Oaks, CA Comments at 6; Citrus County, FL Comments at 1-2; Joint AG Comments at 2; NATOA Comments at 40-41; MCATC Comments at 7; Township of Spring, PA Comments at 1; Cox Comments at 5; National Cable Television Association ("NCTA") Comments at 2; Fleischman and Walsh Comments at 51.

[67]See, e.g., Connecticut Attorney General Comments at 7.

[68]47 U.S.C. § 543(b)(2)(B).

[69]Id. at § 543(a)(5).

uniform nationwide basic rate formula rather than leaving it to each individual franchising authority to choose its own formula. Otherwise, a patchwork of wildly different local basic rate standards would result, in direct contravention of the 1992 Cable Act's mandate that such regulations "shall seek to reduce the administrative burdens on subscribers, cable operators, franchising authorities, and the Commission."[70]

At least one party favored an approach whereby price caps would be applied, presumably to both rate increases for systems with rates below the benchmark seeking to raise rates to the benchmark, and for systems with rates at the benchmark seeking annual or other rate increases.[71] However, as the Commenters have explained, a price cap approach would wrongly penalize "good actors," i.e., cable operators who keep basic rates at or below the benchmark.[72] Furthermore, as the NAB's comments recognized, price caps would give cable operators incentives to reduce quality and service, such as customer service, a result that is viewed as undesirable.[73]

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[70]Id. at § 543(b)(2)(A). The Connecticut Attorney General alleges that cost-of-service regulation is not unduly burdensome. Connecticut Attorney General Comments at 7. Connecticut, where cable rates are regulated by the state PUC, is in no position to opine as to the burdens of cost of service regulation on local franchising authorities that do not have a similar level of experience and resources. Rather, the Commission should follow the directive of the many individual franchising authorities who filed comments advocating a benchmark approach.

[71]Bell Atlantic Comments at 4.

[72]Fleischman and Walsh Comments at 61.

[73]J. Haring, J. Rohlfs, and H. Shooshan III, "Efficient Regulation of Basic-Tier Cable Rates," submitted with NAB Comments at 8-9.

2. A Per-Channel Benchmark Is The Most Appropriate Alternative.

Even though a broad cross-section of commenters preferred the benchmark alternative, there was disagreement on the most appropriate benchmark to choose. Some commenters preferred a cost-based benchmark.[74] However, as the Commenters have explained, such a benchmark would suffer from precisely the same drawbacks as a cost-based rate of return regulation.[75] There was also some support among cities for a benchmark based solely on the rates charged by cable systems subject to effective competition.[76] However, as we explained in our comments, a benchmark based solely on communities meeting the stilted statutory definition of effective competition has serious weaknesses and is highly flawed. The sample of systems subject

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[74]See, e.g., State of New Jersey Board of Regulatory Commissioners Comments at 7; NAB Comments at 14.

[75]Fleischman and Walsh Comments at 60.

[76]See, e.g., City of Thousand Oaks, CA Comments at 13-16; NATOA Comments at 40-41; Schaumburg, IL Comments at 8; Joint AG Comments at 2. Pennsylvania's proposal would limit the benchmark to rates charged by cable systems facing effective competition from overbuilders only. Other tests for satisfying effective competition under the 1992 Cable Act are totally ignored, presumably because they fail to produce results desired by certain regulatory bodies. Citing Allentown, PA as an example, the Joint AGs suggest that the monthly rate allowed by the benchmark formula should be in the thirty-one to thirty-four cents per channel range. However, this analysis ignores certain unique characteristics of the Allentown overbuild which make it an unsuitable model for competitive pricing. First, Allentown is an extremely high density area. Second, both competing systems are family owned businesses with low overhead. Third, both systems continue to serve their own substantial core areas adjacent to Allentown which have not been overbuilt by the competing operator. If the Joint AGs seek overbuild models, they should examine the cities of Northwest Phoenix and Mesa, AZ, whose basic rates are illustrated in this section, infra.

to effective competition (especially from overbuilds) is too small, and the data obtained from systems that face effective competition due to low penetration is likely skewed due to low density, a small subscriber base, and other demographic factors that characterize such systems.[77]

In our comments, we suggested a per-channel benchmark based either on current basic rates or rates as of December 31, 1975, appropriately adjusted, in order to achieve two key 1992 Cable Act goals: it would be relatively simple to establish and administer, and, so long as it is not coupled with an overall cap on the basic service rate, it would give cable operators incentives to add programming to basic service beyond the statutorily required minimum.[78]

3. The Per-Channel Benchmarks Proposed By Some Cities And The NAB Have No Basis In Reality.

Other groups agreed that a per-channel benchmark would be appropriate, although they proposed widely differing per-channel rates.[79] For example, NAB concluded that a sixteen-channel basic service on a forty-channel cable system should cost an average of $4.52, or twenty-eight cents per channel.[80] Similarly, the

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[77]Fleischman and Walsh Comments at 56-57.

[78]Id. at 51-53.

[79]See, e.g., NAB Comments at 14-19; Austin, TX Comments at 49 (proposing a per-channel benchmark during temporary transition to cost-based regulation); City of Tallahassee, FL Comments at 2.

[80]NAB Comments at 19. NAB's proposal does not appear to provide for a reasonable profit. Likewise, the New York State Consumer Protection Board asserts that the Commission can decline to allow the cable operator to achieve a reasonable profit if the Commission finds that the system's rates are not reasonable. New York State Consumer Protection Board Comments at 8. Both

cities of Austin, TX advocate a benchmark rate of thirty-two cents per channel for both basic and non-basic service.[81] This amount is purportedly based, among other things, "on rate data from communities that are faced with effective competition."[82]

However, the NAB study, attached as Appendix A to its comments, contains numerous egregious errors regarding cost calculations. For example, Section I of Appendix A, "Estimate of Non-Capital Costs," derives a figure for Adelphia Communications Corporation's "monthly per-sub expense" by dividing Adelphia's "annual operating expense" ($66.01M) by Adelphia's "basic subs" (1.149M). However, while the 1.149M subs represent all Adelphia subscribers from both its public and private entities, the annual operating expenses figure, which according to Appendix A comes from the June 1992 Cable TV Financial Databook, is based only on Adelphia's public entity, Adelphia Communications Corporation, which had only 750,000 subscribers at the time. Accordingly, Appendix A grossly understates Adelphia's "monthly per-sub expense." Moreover, at least as pertains to Adelphia, the annual data used in Section I is well over two years old. The $66.01M

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proposals clearly violate the 1992 Cable Act and contravene Congressional intent that cable operators are entitled to a reasonable profit, and that basic rates not be confiscatory. See 47 U.S.C. § 543(b)(2)(C)(vii); H.R. Conf. Rep. No. 862, 102d Cong., 2d Sess. 63 (1992) ("Conf. Report") ("[t]he conferees agree that the cable operators are entitled to earn a reasonable profit"); House Report at 82 (expressing Congress' intent "to permit cable programmers to be fairly compensated for the service they provide"); 138 Cong. Rec. S14583 (Sept. 22, 1992) (statement of Sen. Lieberman); Notice at nn.66, 79.

[81]Austin, TX Comments at 11.

[82]Id.

"annual operating expense" figure was current for the 12 month period ending March 31, 1991. Even if the NAB had not bungled the comparison of subscribers with annual operating expense, the use of over two year old expense figures cannot yield an appropriate basic rate in 1993.

Similarly, Section II of Appendix A of the NAB study, "Estimate of Capital Costs," is grossly inaccurate. For example, the "New-Build Expenditures" line item ($651M) in "Cable Construction Costs," which again utilizes outdated 1991 data culled from the June 1992 Cable TV Financial Databook, includes only the incremental cost of adding new subscribers, i.e., wires and poles. Such figure fails to account for cable system infrastructure costs associated with reaching new homes, such as office expense, computers, buildings, headend equipment, etc. These infrastructure costs ignored by NAB would at least double the capital cost figure cited in Appendix A of NAB's study.

Two examples based on data provided by the Arizona Cable Television Association, one of the Commenters herein, demonstrates how the proposals of NAB and Austin, TX bear no relation to reality. Both examples are cases of cable systems facing effective competition due to overbuilds, which, as we noted, a number of cities cited as the only "true" measure of competition.

EXAMPLE 1 -- N.W. PHOENIX, AZ

Cable Operator #1

Number of channels offered on basic --	15
Basic rate --	$10.95
Basic rate per channel --	$ .73

Cable Operator #2

Number of channels offered on basic --	34
Basic rate --	$22.00
Basic rate per channel --	$ .65

EXAMPLE 2 -- MESA, AZ

Cable Operator #1

Number of channels offered on basic --	15
Basic rate --	$10.95
Basic rate per channel --	$ .73

Cable Operator #2

Number of channels offered on basic --	12
Basic rate --	$7.95
Basic rate per channel --	$ .66

As these examples demonstrate, even where there is head-to-head competition between overbuilders, which is but one of the three tests of effective competition under the statute, basic rates are far higher than the figures provided by NAB or Austin, TX.[83] However, these examples are not intended to endorse a

[83]Cable operator #1 in Examples 1 and 2, with a fifteen-channel basic service on a forty-three-channel system, is especially similar for comparison purposes to NAB's "typical" cable system providing sixteen basic channels on a forty-channel system.

benchmark based upon rates charged by systems facing effective competition. As the Commenters have indicated above in these reply comments, such a benchmark is flawed. Rather, the examples are intended primarily to demonstrate that the proposed rates submitted by NAB and Austin, TX are highly unrealistic and undoubtedly confiscatory.[84] If, however, the Commission were to choose a benchmark based on rates charged by systems subject to effective competition, the above discussion and examples make clear that anomalous overbuild situations such as Allentown, PA should be disregarded so as not to inaccurately skew the benchmark. Again, this raises the problem that the sample of mature overbuilds is simply too small for this benchmark.

The Commission has sent detailed survey forms to hundreds of cable systems for the very purpose of gathering the information necessary to establish an appropriate benchmark rate. Accordingly, it would be premature for the Commission to consider any specific benchmark basic rates at this time, especially irrational figures being bandied about by broadcasters or cities, who, at best, each have a parochial interest in requiring confiscatory rates without any regard for a fair return on investment. From the NAB's perspective, rates less than half of even overbuild examples would destroy the ability of cable operators to continue to offer diverse programming and improved

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[84]MCATC concurs that the Commission should emphasize objectively determining reasonable rates rather than emphasizing a reduction in rates, as NAB and Austin, TX would obviously desire. MCATC Comments at 9. By implication, therefore, a reasonable rate does not necessarily require a reduction from existing levels.

facilities, which the NAB obviously hopes would reverse the competitive impact of cable on broadcasters. Thus, while the Commenters advocate a benchmark approach, the Commission should proceed with caution, after it has gathered and examined the extensive information requested in its surveys.

4. Benchmark Alternatives.

As the Commenters have explained, a benchmark based solely on data from communities facing effective competition, as defined in the 1992 Cable Act, is highly flawed. Rather, the Commenters instead advocated a per-channel benchmark based on either current average rates or past regulated rates from approximately December 31, 1975 (when the typical basic service offering was very similar to that required by the 1992 Cable Act), adjusted for inflation.[85] However, we recognize that rates charged by systems subject to effective competition is one of the factors the Commission must take into account in establishing its basic rate formula.[86] Accordingly, if the Commission is uncertain based on the record gathered which of these proposals is more appropriate, the Commission could use all three benchmarks and average them. This solution should allay any fears that current average rates would create a benchmark that is too high. Specifically, as we have explained, Congress has recognized that only some, but certainly not all, current basic rates may be unreasonable.[87]

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[85]Fleischman and Walsh Comments at 57-60.

[86]See 47 U.S.C. § 543(b)(1).

[87]Fleischman and Walsh Comments at 60; House Report at 31, 33.

Combining current average rates with past regulated rates (adjusted appropriately) and rates charged by systems subject to effective competition in an average to establish a basic rate benchmark would thus zero in on those few systems, if any, currently charging basic rates above a reasonable level, as Congress intended. Of course, even such systems should be given an opportunity to either adjust their basic service to meet the benchmark, or to justify their rates through cost or other data.

5. Benchmark Variables.

In their comments, the Commenters explained why the following variables are relevant to and should be included in the Commission's basic rate benchmark: activated channel capacity; density (number of subscribers per route mile); age of plant; percent of aerial vs. underground cable; system size (number of subscribers); MSO size; off-air broadcast signal availability; and regional cost of labor index.[88] We believe that these variables are necessary to create "a matrix or table"[89] that sufficiently differentiates cable systems with differing characteristics that affect their basic rates. At the same time, we believe that these categories would not be too complex to establish, and would thus not violate the statute's directive to keep administrative burdens on all parties, including the Commission, to a minimum.[90] Finally, we note that there was significant agreement on many of these categories, by both the

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[88]Fleischman and Walsh Comments at 53-56.

[89]Notice at ¶ 37.

[90]47 U.S.C. § 543(b)(2)(A).

Commission in its Notice[91] and by many other parties. Thus, a benchmark based on the above-listed variables would have the added benefit of a lack of controversy surrounding it, which should help lead to better compliance and fewer disagreements, which can take up valuable resources at both the local and Commission level.

D. Regulation Of Rates For Equipment.

1. Only Equipment Used Solely To Receive Basic Service Is Regulated Based On Actual Cost.

Congress intended that only customer equipment used solely to receive basic service, not equipment used to receive basic plus higher service levels, is to be priced on the basis of actual cost.[92] Other parties agreed with this position.[93] Some parties, however, argued that all cable equipment should be subject to actual cost pricing, even if such equipment is used to receive tiered cable programming services or unregulated premium programming in addition to basic.[94] For instance, the Village of Schaumburg, IL complained that if basic and non-basic equipment were regulated differently, confusion would arise where "equipment is used for both basic and cable programming service," and that cable operators could raise rates for equipment used to receive non-basic service "to make up for perceived lost revenue

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[91]Notice at ¶ 37.

[92]Fleischman and Walsh Comments at 63-72.

[93]See, e.g., Time Warner Comments at 48-56; NCTA Comments at 49; Tele-Communications Inc. ("TCI") Comments at 30-31.

[94]See, e.g., State of New Jersey Board of Regulatory Commissioners Comments at 23; NATOA Comments at 48-49; Schaumburg, IL Comments at 9.

from equipment used for basic service."[95] However, the Commenters explained in detail in their comments that equipment used for both basic and non-basic service has been distinguished in the past by the Commission and the U.S. Copyright Office, and was clearly intended by Congress to be treated separately from equipment used exclusively by basic-only subscribers.[96] Moreover, as to Schaumburg's second point, this fear is unfounded. Any rate increase for equipment used to receive a tier above basic would be subject to scrutiny pursuant to the 1992 Cable Act's "unreasonable" standard for non-basic rates.[97] Moreover, if the equipment is used to descramble premium or other a la carte services (such as an addressable descrambler), the rental price of the equipment is unregulated along with the underlying service, even if the equipment also incidentally allows basic and cable programming service signals to pass to the customer's television receiver.

Likewise, NATOA bases its view that both basic and non-basic equipment should be regulated at actual cost on the fact that the language of the 1992 Cable Act was changed to equipment "used" to receive basic service from equipment "necessary" for the receipt of basic service.[98] The State of New Jersey Board of Regulatory

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[95]Schaumburg, IL Comments at 9.

[96]Fleischman and Walsh Comments at 63-68.

[97]47 U.S.C. § 543(c).

[98]NATOA Comments at 47-48.

Commissioners takes a similar view, without giving any reason.[99] However, as the Commenters pointed out in their comments, the change was made to mirror the equipment language in the 1992 Cable Act's "cable programming service" definition, which also speaks in terms of equipment "used" to provide cable programming service, and to give the FCC greater flexibility. There is no indication in the legislative history that this language change was intended to direct the FCC to subject equipment capable of receiving both basic and non-basic services to the more restrictive test for basic-only equipment.[100]

The FCC must consider several uncontroverted facts. First, a subscriber must buy basic service as a condition to the purchase of any other tier of service.[101] Second, cable operators do not and have not provided separate equipment to a subscriber used exclusively to receive non-basic tiers while the basic service is received by that subscriber through a separate piece of equipment. Such a configuration would be decidedly consumer unfriendly. If Congress intended to apply the "actual cost basis" test to all equipment simply because such equipment allows the required basic service to be received by subscribers, Congress would not have simply substituted "used" in place of "necessary" in Section 623(b)(3)(A). Rather, it would have eliminated the phrase "to receive basic service" from that

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[99]See State of New Jersey Board of Regulatory Commissioners Comments at 23-24.

[100]Fleischman and Walsh Comments at 66.

[101]47 U.S.C. § 543(b)(7)(A).

section and it would not have included installation and equipment used for non-basic service in the definition of "cable programming service" subject to bad actor review pursuant to Section 623(c).

Similarly, as the Commenters explained in their comments, Section 623(b)(3)(A) of the 1992 Cable Act, which requires pricing based on actual cost for equipment used by basic-only subscribers to receive pay programming under the buy-through clause,[102] would be superfluous if Congress had intended all equipment to be priced based on actual cost.[103]

2. Equipment Rates Should Be Deregulated Where Competition From Independent Suppliers Exists.

The Commenters have advocated an "effective competition" test for basic equipment, installations, and additional outlets ("AOs") whereby such rates would be deregulated where the cable operator certifies and advises subscribers that such equipment is available for sale or lease from third parties.[104] There appears to be little opposition to this proposal. In fact, comments of parties on all sides of the issue can be read to support the Commenters' position. For example, MCATC has endorsed the concept that competition would eliminate the need for regulation of equipment rates, particularly with regard to remote controls. To this end, MCATC proposes an equipment competition test whereby cable operators would be prohibited from discriminating against

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[102]Id. at § 543(b)(3)(A)(2).

[103]Fleischman and Walsh Comments at 64-65.

[104]Id. at 56-58.

subscribers who use their own remote controls, would be required to make available to such subscribers the infrared signal needed to access the operator's channel selector, and would be permitted to charge a reasonable rate for such infrared signal service, but the remote control service rate would not be tied to lease of the remote control unit.[105] MCATC's proposal is fully consistent with the Commenters' effective competition test for equipment, and it appears to be a reasonable alternative.

Moreover, various parties stated that subscribers have the right to purchase equipment from other sources, and some parties called for the Commission to require cable operators to inform subscribers of their right and ability to do so.[106] These parties obviously recognize that in many instances, "effective competition" exists in the market for equipment -- there would be no reason to request the notification to subscribers of independent equipment sources unless such sources actually existed. Thus, the Commenters would have no objection to a requirement that cable operators inform subscribers of their right to purchase or lease equipment from independent sources, as long as such requirement was part of a standard that deregulates the rates for such equipment since its availability obviously would be subject to "effective competition." There is simply no

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[105]MCATC Comments at 12-13. This proposed test also supports the Commenters' point in Section II.D.3, infra, that certain equipment components, especially remotes and converters, operate as one functional unit and, thus, should be able to be marketed together.

[106]See, e.g., City of Thousand Oaks, CA Comments at 23; Austin, TX Comments at 56.

rational basis to regulate rental prices for equipment supplied by a cable operator in any instance where consumers are free to purchase or lease equivalent equipment from third party vendors.

3. Cable Operators Should Be Permitted To Bundle The Marketing Of Various Equipment Components.

As the Commenters have explained, while the separate tests established for the service and equipment components of basic service might suggest an intent that they be unbundled,[107] there is no evidence in the 1992 Cable Act or its legislative history that Congress intended to unbundle rates for various equipment components, such as converters and remotes, or installations and AOs, under either the basic or non-basic tests.[108] The Commission, however, appears to take a contrary view, at least regarding the bundling of equipment and installations.[109] Some parties agreed with the Commission on this point.[110] This overbroad view of bundling misreads the 1992 Cable Act. For example, NATOA correctly observes that the statute regulates installation and equipment under a single standard, but then curiously states that such standard requires installations and equipment to be priced separately.[111] Such a conclusion has no

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[107]Conversely, the inclusion of equipment, installation and programming service in the definition of "cable programming service" cannot be read to preclude bundling of non-basic equipment and services.

[108]Fleischman and Walsh Comments at 75.

[109]Notice at ¶ 63.

[110]See, e.g., Austin, TX Comments at 55; NATOA Comments at 46.

[111]NATOA Comments at 46.

foundation in the 1992 Cable Act. Even the Commission's Notice recognizes that the statute does not mandate unbundling of installation from the lease of equipment -- the Commission merely takes the preliminary view that such practice should be encouraged to increase competition in the market for equipment and installations.[112]

As a policy matter, the Commission's view that unbundling of equipment and installations would lead to increased competition is purely speculative. As the Commenters pointed out and as other parties agreed, a competitive market already exists in this area, and there is no evidence that its development is being hindered by cable operator equipment marketing methods.[113] For instance, as NCTA recognizes, "[e]lectronics stores vigorously advertise the availability of 'universal remotes,' which can be used not only with cable television converter boxes but also with video cassette recorders, audio equipment and other electronic devices."[114]

As we explained, moreover, different equipment components are often treated as one functional unit (such as a converter coupled with a remote), whereby one component is useless without the other.[115] Mandatory unbundling of converters and remotes makes no more sense than requiring cordless phone handsets to be

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[112]Notice at ¶ 63.

[113]Fleischman and Walsh Comments at 81-82; Time Warner Comments at 64; NCTA Comments at 46.

[114]NCTA Comments at 46.

[115]Fleischman and Walsh Comments at 75-76.

sold separately from the base unit. Furthermore, certain equipment components are logically marketed together. For example, the most logical (or at least the first) time to discuss connecting additional equipment or AOs in a household occurs when the cable operator is marketing the initial installation to the subscriber. Where the statute and legislative history do not prohibit bundling of different equipment components, and where the Commission's goal of a competitive market is already being achieved, the Commission should not interfere with logical and legitimate cable operator marketing practices.

4. Cable Operator Charges For Installations, Equipment, AOs, and Service Calls Should Be Evaluated in a Single Equipment "Basket."

As is the case with marketing various equipment components in a bundle, the Commenters also explained that cable operator charges for basic equipment, installation, service calls, and AOs should be evaluated in a single equipment "basket," separate from basic cable programming service. The entire equipment basket, instead of each individual equipment component, should be subject to the statute's rate regulation standards.[116] This basket concept is entirely different from bundling of equipment and installations, or other equipment components. Whether or not various equipment components are marketed in a bundled fashion, the overall charges for such equipment components should be viewed as a whole when being scrutinized for reasonableness.

[116]Fleischman and Walsh Comments at 82-84.

As the Notice recognized, cable operators typically price some equipment components, such as installations, below cost.[117] This type of pricing increases penetration by attracting subscribers who might not otherwise subscribe because they would be deterred if installations were priced at the operator's full cost.[118] Accordingly, cable operators should be able to continue the pro-consumer practice of charging below cost for installations, and should be able to make up for the loss through charges for other equipment components, so long as the overall "basket" of equipment revenues falls within the appropriate benchmark. Otherwise, penetration would decline, and the operator would have to raise all rates because its costs would be spread over fewer subscribers. As the Commenters have explained, such a "basket" approach is permitted by the 1992 Cable Act, and would be fair to consumers so long as their overall cable bill was reasonable, regardless of the mix of individual equipment charges. [119]

E. Costs Of Franchise Requirements And Subscriber Bill Itemization.

The parties responding to the Commission's inquiries regarding costs of franchise requirements[120] and subscriber bill itemization[121] took sharply contrasting stances on the

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[117]Notice at ¶ 70.

[118]Fleischman and Walsh Comments at 83.

[119]Id. at 82-83

[120]47 U.S.C. § 543(b)(4); Notice at ¶¶ 72-73.

[121]47 U.S.C. § 542(c); Notice ¶¶ 174-75.

interpretation of the provisions. The Commenters urge the Commission, in analyzing the conflicting views on the meaning of government cost itemization, to adopt rules that meet Congress' intent with respect to the language actually enacted.

To begin, the plain language of Section 622(c) states that a cable operator may identify "as a separate line item on each regular bill of each subscriber" the amount of the total bill assessed as a franchise fee, the amount of the total bill assessed to satisfy any franchise requirements to support PEG channels, and the amount of any other fee, tax, assessment, or charge of any kind imposed by any governmental authority on the cable operator-subscriber transaction.[122] As the Commenters and several others have asserted, Congress enacted this provision to provide an openness in billing that would result in subscriber protection by allowing for greater public knowledge and scrutiny of governmental levies on subscribers of cable service, and greater political accountability for such increased financial burden.[123] Furthermore, if the Commission adopts a benchmark approach to rate regulation, itemized billing will assure that some cable operators with otherwise comparable circumstances are

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[122]47 U.S.C. § 542(c).

[123]See Fleischman and Walsh Comments at 85; Continental Comments at 76-77, 79; MFA Comments at 21 ("One of the best means of addressing this concern of Congress [protection of cable subscribers] is to improve the quality of information that the cable industry makes available to subscribers concerning the costs of cable service.").